JOHN T. FEY, Cle

IN THE

Supreme Court of the United States

OCTOBER TERM, 1956.

No. 775

SCHENLEY DISTILLERS, INC. and JOSEPH S. FINCH AND COMPANY,

Appellants,

v.

JOHN H. BINGLER, United States District Director of Internal Revenue for the Pittsburgh Internal Revenue District,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

STATEMENT AS TO JURISDICTION

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INDEX.

	PAGE
STATEMENT AS TO JURISDICTION	1
OPINION BELOW	1
JURISDICTION	2
QUESTIONS PRESENTED	5
STATEMENT	6
The Irreparable Damage and Destruction of Property with Which the Appellants are Threatened	7
The Production, Marketing and Taxation of Distilled Spirits	10
The Over-Supply of Distilled Spirits	12
The Destructive Impact of the Force-Out Provision	14
The Bases for Appellants' Challenge of the Force-Out Provision	16
THE QUESTIONS ARE SUBSTANTIAL	18
Section 7421 is Inapplicable Because the Injunction Sought Would Not Interfere with the Collection of Revenue	20
Even If, Contrary to the Fact, the Appellants Were Seeking to Enjoin the Collection of a Tax, Section 7421 Would Not be Applicable in the Special and Extraordinary Circumstances of This Case	24
CONCLUSION	32
APPENDIX A—OPINION	

TABLE OF CASES.

	PAGE
Allen v. *Regents*, 304 U. S. 439 (1938)	25, 26, 27
A. P. W. Paper Co. v. *Riley*, 12 F. Supp. 738 (N. D., N. Y. 1935)	26, 27
Bailey v. *George*, 259 U. S. 16 (1922)	25
Baltic Mills Co. v. *Bitgood*, 12 F. Supp. 132 (D. Conn. 1935)	26, 27
Brushaber v. *Union Pac. R. R.*, 240 U. S. 1 (1916)	23
Cotting v. *Kansas City Stock Yards Co.*, 183 U. S. 79 (1901)	30
Coty v. *Prestonettes, Inc.*, 285 Fed. 501 (2d Cir. 1922)	32
Danahy Packing Co. v. *McGowan*, 11 F. Supp. 920, 12 F. Supp. 457 (W. D. N. Y. 1935)	28
Dodge v. *Osborn*, 240 U. S. 118 (1916)	24, 25
Driscoll v. *Jones*, 19 F. Supp. 792 (N. D. Okla. 1937)	25, 27
Ex parte Young, 209 U. S. 123 (1908)	30
Fontenot v. *Accardo*, 278 Fed. 871 (5th Cir. 1922)	22
G. B. R. Smith Milling Co. v. *Huston*, 12 F. Supp. 554 (S. D. Iowa 1935)	26
Georgia Railroad & Banking Co. v. *Redwine*, 342 U. S. 299 (1952)	2
Gold Medal Foods v. *Landy*, 11 F. Supp. 65, 12 F. Supp. 406 (D. Minn. 1935)	26, 27
Graham v. *du Pont*, 262 U. S. 234 (1923)	24, 25
Hill v. *Wallace*, 259 U. S. 44 (1922)	22, 25, 26, 27
In re Processing Tax Case, 13 F. Supp. 218 (W. D. Tex. 1935)	27
Inland Milling Co. v. *Huston*, 11 F. Supp. 813, 12 F. Supp. 554 (S. D. Iowa 1935)	26, 28
John A. Gebelein, Inc. v. *Milbourne*, 12 F. Supp. 105 (D. Md. 1935)	27
John M. Hirst & Co. v. *Gentsch*, 133 F. 2d 247 (6th Cir. 1942)	25, 27

PAGE

Leonardi v. *Goldberg*, 76 F. Supp. 747 (D. N. J. 1941) 27
Liberis v. *Nee*, 10 F. Supp. 336 (N. D. Fla. 1935) 22
Lipke v. *Lederer*, 259 U. S. 557 (1922) 22, 27
Long v. *Kelly*, 100 F. Supp. 235 (M. D. Ala. 1951) 25, 27

Matcovich v. *Nickell*, 134 F. 2d 837 (9th Cir. 1943) 24
McMullin v. *Sheehan*, 95 F. 2d 129 (8th Cir. 1938) 24
Midwest Haulers v. *Brady*, 128 F. 2d 496 (6th Cir. 1942) 25, 27
Miller v. *Standard Nut Margarine Co.*, 289 U. S. 498 (1932) 21, 24, 25, 27, 28
Mitsukiyo Yoshimura v. *Alsup*, 167 F. 2d 104 (9th Cir. 1948) 25, 27
Mulford v. *Smith*, 307 U. S. 38 (1939) 22

Neild Mfg. Corp. v. *Hassett*, 11 F. Supp. 642 (D. Mass. 1935) 28

Oklahoma Natural Gas Co. v. *Russell*, 261 U. S. 290 (1923) 2
Oklahoma Operating Co. v. *Love*, 252 U. S. 331 (1920) 30, 31

Pabst v. *Campbell et al.*, Civil No. 1P56-C-226, S. D. Indiana, October 5, 1956 26
Parker v. *Winnipiseogee Lake Cotton & Woollen Company*, 67 U. S. 545 (1862) 32
Pocahontas Fuel Co. v. *Early*, 13 F. Supp. 605 (W. D. Va. 1935) 26
Pollock v. *Farmers' Loan & Trust Co.*, 157 U. S. 429 (1895), rehearing 158 U. S. 601 (1895) 23

R. C. Tway Coal Co. v. *Glenn*, 298 U. S. 238 (1936) 22
Regal Drug Co. v. *Wardell*, 260 U. S. 386 (1922) 22, 27
Rickert Rice Mills, Inc. v. *Fontenot*, 297 U. S. 110 (1936) 27

Sanders v. *Andrews*, 121 F. Supp. 584 (W. D. Okla. 1954), rev'd on other grounds, 225 F. 2d 629 (10th Cir. 1955) 25
Snyder v. *Marks*, 109 U. S. 189 (1883) 24

Terrace v. *Thompson*, 263 U. S. 197 (1923) 30
Tovar v. *Jarecki*, 173 F. 2d 449 (7th Cir. 1949) 22

United States v. *Rizzo*, 297 U. S. 530 (1936) 22

Statutes.

	PAGE
Internal Revenue Code of 1954	
Section 5006(a)(2)	2, 4, 5
Section 5011	8
Section 5061(a)	2, 4, 5
Section 5194(f)	8
Section 7421	5, 18, 19, 20, 23, 24, 29
Title 28, United States Code (1952)	
Section 1253	2, 29
Section 2101(b)	2
Section 2282	2
Section 2284	2, 29
Internal Revenue Code of 1939	
Section 2879(b)	3

Constitution of the United States.

Article I:	
Section 2, Clause 3	2, 6, 17
Section 9, Clause 4	2, 6, 17
Fifth Amendment	2, 6
Tenth Amendment	2

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v.

JOHN H. BINGLER, UNITED STATES DISTRICT DIRECTOR OF INTERNAL REVENUE FOR THE PITTSBURGH INTERNAL REVENUE DISTRICT,

Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

STATEMENT AS TO JURISDICTION.

Pursuant to Rules 13 (2) and 15 of the Rules of the Supreme Court of the United States, the appellants submit this Statement to show that the Supreme Court has jurisdiction of this direct appeal and that substantial questions are presented.

Opinion Below.

The opinion of the District Court is reported at 145 F. Supp. 517. A copy of the opinion, marked Appendix A, is attached to this Jurisdictional Statement.

Jurisdiction.

The appeal herein is from a final judgment made and entered by the United States District Court for the Western District of Pennsylvania, specially constituted under 28 U. S. C. §§2282 and 2284 (1952) upon the appellants' application for a permanent injunction to restrain the enforcement, operation or execution of certain Acts of Congress as hereinafter set forth, for repugnance to Article I, Section 2, clause three and Article I, Section 9, clause four of the Constitution of the United States, and to the Fifth and Tenth Amendments to said Constitution.

The final judgment appealed from was made and entered on October 18, 1956. Notice of appeal was filed in the United States District Court for the Western District of Pennsylvania on December 17, 1956.

The Supreme Court of the United States has jurisdiction to review by direct appeal the judgment complained of by virtue of the provisions of 28 U. S. C. §§1253 and 2101 (b) (1952).

The following decisions among numerous others are believed to sustain the jurisdiction of the Supreme Court to review the judgment on direct appeal in this case: *Georgia Railroad & Banking Co.* v. *Redwine,* 342 U. S. 299 (1952); *Oklahoma Natural Gas Co.* v. *Russell,* 261 U. S. 290 (1923).

The statute of the United States that is involved is the Internal Revenue Code of 1954, 68A Stat. 3, 26 U. S. C. §1 *et seq.* The particular sections of the 1954 Code involved are Section 5006 (a) (2), 68A Stat. 599, 26 U. S. C. §5006 (a) (2) (Supp. III, 1956), and Section 5061 (a), 68A Stat. 614, 26 U. S. C. 5061 (a) (Supp. III, 1956). The text of these sections is as follows:

"SEC. 5006. DETERMINATION OF TAX.

(a) Requirements.—

* * * * * *

"(2) Distilled Spirits Deposited in Internal Revenue Bonded Warehouses.—*The tax on distilled spirits entered for deposit in internal revenue bonded warehouses shall be determined* at the time the same are withdrawn therefrom and *within 8 years from the date of original entry for deposit therein* (except that distilled spirits which on July 26, 1936, were 8 years of age or older and which were in bonded warehouses on that date, may remain therein). (Emphasis added.)

* * * * * *

"SEC. 5061. METHOD OF COLLECTING TAX.

"(a) Collection by Return.—The taxes on distilled spirits, wines, rectified distilled spirits and wines, and beer shall be paid by return. The Secretary or his delegate shall, by regulation, prescribe the period for which such return shall be filed, the time for filing such return, the information to be shown in such return and the time for payment of such tax: *Provided, however,* That, notwithstanding this subsection, the taxes shall continue to be paid by stamp until the Secretary or his delegate shall by regulations provide for the payment of the taxes by return."*

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* No such regulations providing for a return system have been promulgated, and distilled spirits taxes "continue to be paid by stamp" upon withdrawal from bond in advance of eight years or in any event when the spirits have been in bond for eight years, as was provided in Section 2879(b) of the Internal Revenue Code of 1939, 53 Stat. 334. The text of Section 2879(b) was as follows:

"SEC. 2879. DEPOSITS OF SPIRITS IN WAREHOUSES

"(b) Time for Payment of the Tax. The tax on all distilled spirits hereafter entered for deposit in internal revenue bonded warehouses shall be due and payable before and at the time the same are withdrawn therefrom and with-

An injunction was sought in the District Court against the enforcement, operation, or execution of only the italicized part of Section 5006 (a) (2) and of only that part of Section 5061 (a) which requires payment of distilled spirits taxes upon determination of such taxes pursuant to the italicized part of Section 5006 (a) (2). The purported effect of the challenged portions of these statutes is to require that the internal revenue tax on distilled spirits be paid on the day that the spirits reach the age of eight years, even though the spirits are then unmarketable. This purported requirement is commonly referred to by the distilled spirits industry and by the United States Treasury as the "force-out" provision.*

The complaint was filed in February 1956, against the District Director of Internal Revenue for the Pittsburgh Internal Revenue District. A three-judge court was designated, consisting of Circuit Judge Austin L. Staley and District Judges John L. Miller and John W. McIlvaine.

The District Director moved to dismiss the complaint, on the grounds in substance that the force-out provision is constitutional and that in any event the issues cannot be tried in an injunction proceeding. Affidavits and other materials relating to additional and incidental matters were submitted in support of this motion. The controlling facts as set out in the complaint were not controverted. Answering affidavits were submitted by the appellants. All of these documents are included in the record before this Court.

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in eight years from the date of the original entry for deposit therein; and warehousing bonds hereafter taken under the provisions of the internal revenue laws shall be conditioned for the payment of the tax on the spirits as specified in the entry before withdrawal from the internal revenue bonded warehouse, and within eight years from the date of said entry."

* Complaint, par. 7.

Following the submission of briefs, oral argument was heard in June 1956. On October 18, 1956, the District Court entered judgment dismissing the complaint. In its accompanying opinion and without discussion of the merits of the constitutional issues, the District Court held that the suit for injunction was barred by that provision of the Internal Revenue Code of 1954 (Section 7421*) which provides in pertinent part that "* * * no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court."

Questions Presented.

1. Whether the appellants have stated grounds for an injunction against the enforcement of the "force-out" provision of the Internal Revenue Code of 1954 (Sections 5006(a)(2) and 5061(a) and regulations thereunder), which provision purports to require that the internal revenue tax on distilled spirits, at a rate which is in fact more than five times the then accumulated cost of the spirits, be paid on the day that the spirits reach the age of eight years, even though the spirits are then unmarketable.

2. Whether the injunction sought by the appellants, being against the threatened enforcement of a provision (the force-out provision) which serves no revenue purpose and in fact causes hundreds of millions of dollars of revenue loss to the United States Treasury, is prohibited by that provision of the Internal Revenue Code of 1954 (Section 7421) relating to injunctions in tax cases.

3. Whether the threatened outright destruction of property and other irreparable damage shown by the

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* 68A Stat. 876, 26 U. S. C. §7421 (Supp. III, 1956).

appellants, inflicted as they allege by the force-out provision in violation of the direct tax and the due process provisions of the Constitution of the United States, (Article I, Section 2, clause three, Article I, Section 9, clause four, and the Fifth Amendment), constitute special and extraordinary circumstances entitling the appellants to equitable relief, in view particularly of the fact that, by reason of subsequent evaporation of tax-paid spirits and other unavoidable economic factors inherent in the nature of the industry, payment of the millions of dollars of force-out taxes with which the appellants are threatened, in order to seek a remedy by suit for refund thereof, would involve risks of loss far greater than even the outright destruction of the spirits before their eighth anniversary, as provided for in the Internal Revenue Code of 1954.

Statement.

The appellants Schenley Distillers, Inc. and Joseph S. Finch and Company are distillers, owners or warehousemen of distilled spirits stored in bond in Internal Revenue Bonded Warehouses in the Pittsburgh Internal Revenue District. The appellant Joseph S. Finch and Company (hereinafter called Finch) is the owner of all of the distilled spirits involved in this action. Finch is also the proprietor of two of the three Internal Revenue Bonded Warehouses in which the said spirits are stored. The appellant Schenley Distillers, Inc. (hereinafter called Schenley) is the proprietor of the third such Warehouse. Although Schenley is not itself the owner of any of the spirits involved in this action, it has joined in this action because the defendant threatens to proceed against it to collect the challenged

exaction in respect of distilled spirits stored in its Warehouse, including distilled spirits owned by Finch.*

The action challenges the constitutionality of the force-out provision, which as noted above purports to require that the internal revenue tax on distilled spirits, at a rate which is in fact more than five times the cost of the spirits, be paid on the day that the spirits reach the age of eight years, even though the spirits are then unmarketable.

Injunctive relief is sought. Only in that way can the appellants be protected against grave and irreparable damage and destruction which will otherwise be inflicted upon them, in ever-increasing amounts, so long as the defendant is in a position to continue to threaten the enforcement of the force-out provision.

The Irreparable Damage and Destruction of Property with which the Appellants are Threatened.

When the complaint was filed, Finch owned in the Pittsburgh Internal Revenue District 1,200,000 tax gallons of distilled spirits which would reach the force-out date during the first six months of 1956.** It was apparent at that time, for reasons noted below at pages 12-15, (a) that large amounts of such spirits would not be marketable, at any price, prior to the force-out dates; (b) that Finch would be unable to pay the tax on such amounts on the force-out dates and hold them in the hope of a later market; and (c) that unless the threatened enforcement of the exaction were enjoined, Finch would have no alternative but

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* Complaint, pars. 17, 22, 23.

** Complaint, par. 23.

to destroy such property in order to avoid the prohibitive exaction.*

Later events have confirmed the accuracy of that forecast. The record shows that during the first five months of 1956 Finch was forced to destroy through redistillation almost 300,000 gallons of that whiskey—one-quarter of its total holdings which were within six months of the force-out date at the time the complaint was filed. Finch's investment in that destroyed whiskey was approximately $2.11 per gallon. Even after allowance for the redistillation salvage value of about $0.40 per gallon, the loss thus inflicted upon Finch by reason of the threatened enforcement of the force-out provision was more than $500,000.**

That loss is irreparable. The valuable aged whiskey is gone forever. Finch has no recourse against anyone. No matter how clearly unconstitutional the force-out provision may ultimately be determined to be, Finch never will have any recourse against anyone in respect of that half a million dollars worth of destroyed property.

Moreover, even those huge losses inflicted upon Finch in the first five months of 1956 do not include the large additional losses suffered during that period in other ways, such as through the forced dumping of other gallons of whiskey on the market at prices below costs.***

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* Complaint, pars. 38-53, 63-75.

The Internal Revenue Code of 1954 makes specific provision for the outright destruction of the spirits or for their redistillation. Section 5011. 68A Stat. 604, 26 U. S. C. §5011 (Supp. III, 1956); Section 5194(f), 68A Stat. 635, 26 U. S. C. §5194(f) (Supp. III, 1956). Redistillation, as shown in the Complaint (par. 73) effects a loss of 80% of the value of eight-year-old distilled spirits. No tax is payable in respect of spirits so destroyed or redistilled, if such action is initiated before the spirits reach the age of eight years in bond.

** Seasonwein affidavit of June 22, 1956.

*** Seasonwein affidavit of June 22, 1956, par. 5.

The record further shows that Finch holds still larger amounts of whiskey facing force-out in later months and years. As of June 1956 Finch held 1,650,000 tax gallons approaching force-out in the last half of 1956. 2,558,000 tax gallons will reach the force-out date in the year 1957; 4,213,000 tax gallons in the year 1958; and 1,657,000 tax gallons in the year 1959.*

As to these holdings, the continued threat of enforcement of the force-out provision, if it be not enjoined, will inflict upon Finch damage still more drastic than that already suffered. The complaint demonstrates in detail that the damage heretofore inflicted by the force-out provision is but the beginning.** Even at the rate of destruction suffered by Finch during the first five months of 1956, the destruction inflicted upon it between now and 1959, if the defendant remains in a position to continue to threaten the enforcement of the force-out provision, will run into millions of dollars.

For reasons outlined later in this Jurisdictional Statement (pages 18-32), we earnestly submit that the District Court's dismissal of the complaint, in the face of the foregoing facts, misconceives the purpose and intent of the statutory provision relating to the maintenance of suit for injunction, as that provision has been construed and applied in numerous decisions of this Court. We think that on the record before this Court it is clear that the appellants have stated grounds for an injunction against the enforcement of the force-out provision, and their complaint should not have been dismissed.

Before turning to that discussion, however, there is set out below a brief resume of the background facts, appear-

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* Seasonwein affidavit of June 8, 1956, par. 4.

** Pars. 63-75.

ing in detail in the record before this Court, showing how it is that the very threat of the challenged exaction leaves the appellants with no alternative but to suffer the above-described irreparable and constantly increasing damage and destruction.

The Production, Marketing and Taxation of Distilled Spirits.

Whiskey, which is by far the major item of distilled spirits for beverage purposes, is produced primarily for marketing many years later. Freshly distilled whiskey is not acceptable for consumption purposes. To make it fit for consumption, the raw distilled spirits must be aged by storage in charred oak barrels. For this purpose, following distillation, the barrels are deposited in Internal Revenue Bonded Warehouses. These are privately owned premises under the control of the Internal Revenue Service.*

The original cost of a gallon of whiskey at distillation is $0.45. Placing the whiskey in bond, including the cost of the barrel, increases the cost to a total of about $0.95. At eight years the accumulated cost has risen to about $2.11 per gallon. A principal cause of this increase is that during storage in the barrels the spirits soak into the barrel staves and evaporate, causing a loss at a rate of about two gallons per original 50-gallon barrel per year, and thus constantly increasing the cost for each remaining gallon.**

The costs of raw materials, distillation and storage are only a small part of the total cost of putting distilled spirits on the market. The Internal Revenue Tax is by far the

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* Complaint, pars. 27-29.

** Complaint, par. 32.

major part of the cost. The $10.50 per gallon tax is more than ten times the total investment in the spirits as of the completion of distillation and deposit in bond. It is almost five times the total investment per remaining gallon at the end of eight years.*

In the ordinary operation of the taxing scheme, this huge tax is determined and payable only in conjunction with the marketing of the spirits. The law requires payment when the spirits are withdrawn from bond, and only upon the number of gallons then remaining. Particularly because of the magnitude of the tax, the spirits are voluntarily withdrawn from bond only after the owner has determined that there is a readily available market. The amount of the tax is ordinarily recouped, as part of the purchase price, within sixty days.**

Thus basically and in its ordinary operation the Internal Revenue tax on distilled spirits as established under the Internal Revenue Code of 1954 is an indirect tax levied upon the consumption of distilled spirits. It is obviously a revenue measure. The appellants do not challenge it in any way.***

The challenge goes only to the appendage to the taxing scheme which is known as the force-out provision. Purporting to require payment of the huge tax on the day that the spirits are eight years old, even though there is then no market for them, the force-out provision has a totally different impact both upon the industry and upon the Treasury. Instead of being an indirect tax upon consumption, levied in relation to marketing, it is a direct tax upon the property itself, exacted solely because of the existence,

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* Complaint, par. 31.

** Complaint, par. 35.

*** Complaint, pars. 14-15.

possession and ownership of the property. Instead of producing revenue, it destroys revenue. It forces the owners to destroy their property in order to avoid payment of the prohibitive exaction. The Treasury loses not only the tax on the destroyed spirits, but also income taxes, because of the adverse effect of the provision on the owners' income.*

Although the force-out provision has been a part of the law for many years, it has not until recently been of any crucial significance. The industry has ordinarily been able to market its product in usual course within the limitations of the eight-year rule. It has been inherent in the nature of the situation, however, that sooner or later the numerous unpredictable and uncontrollable factors affecting the extent of the market at any given time would combine in such fashion that the supply of spirits on hand would be greater than could be marketed within the limitations of the eight-year rule. That has now happened.**

The Over-supply of Distilled Spirits.

During World War II the production of distilled spirits for beverage purposes was almost completely prohibited. The result was a marked depletion of inventories.***

Following World War II, there was a marked increase in production with a view to building up the depleted stocks. The outbreak of the Korean conflict in June 1950, and consequent fear that production would again be prohibited, resulted in a further large increase of whiskey inventories. In the fiscal year ending June 30, 1951 whiskey

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* Complaint, pars. 11-15, 90-92.

** Complaint, par. 37.

*** Complaint, par. 38.

production was almost three times the average annual rate of utilization for the preceding five years.*

The anticipated restrictions on production did not occur. More important, the reasonably anticipated post-war increase in domestic whiskey consumption did not materialize either. On the contrary, distillers' sales of domestic whiskey actually decreased by approximately 25%, from 66,000,000 cases in 1946 to about 51,000,000 cases in 1955. On a per capita basis, this decline was about 34%. This decline occurred in spite of an increase of more than 69% in disposable income over the same period, and in spite of an increase of more than 17% in population.**

The principal cause of the defeat of the industry's expectations as to the amount of consumption has been post-war changes in the rate of the Internal Revenue tax on distilled spirits. The spirits now approaching force-out were laid down in the reasonable anticipation of a $6.00 rate. Instead, the rate has been increased to $10.50 since these spirits were laid down. The Internal Revenue tax being by far the largest part of the cost of putting legal distilled spirits upon the market, the rate of the tax is obviously of major importance in determining the extent of the market.***

The result is that the amounts of whiskey in bond in the United States have for some time been and now are in excess of normal requirements.**** The Treasury itself has recognized this, and its published statements showing tens of millions of gallons of excess whiskey approaching force-

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* Complaint, par. 39.

** Complaint, par. 41.

*** Complaint, pars. 42-43.

**** Complaint, par. 45.

out in the years between now and 1959 are quoted in the complaint.*

The threat of exaction of tax at eight years without any market has become of crucial importance.

The Destructive Impact of the Force-out Provision.

To pay the exaction at eight years and hold the spirits in the hope of finding a later market for them is out of the question. The enormous investment which would be required—almost five times the value of the eight year-old spirits—would greatly increase the capital required and the interest on the capital required for continued holding of the spirits. Further, the whiskey would continue to evaporate from the barrels with complete loss of the taxes paid on the evaporated whiskey. These evaporation losses cannot be prevented. The taxes paid on the evaporated gallons could obviously not be recovered through the sale of such gallons, nor could such taxes be recovered by spreading them over the remaining gallons. Such spreading would increase the cost of the remaining gallons to virtually prohibitive levels. Aside from the tax of $10.50 per gallon on remaining gallons, the cost of the whiskey remaining in the barrel at the end of 12 years for example, would be $7.98 per gallon, or almost four times the cost of $2.11 per gallon at eight years.**

There is no conceivably foreseeable mass market willing to pay a price, for older whiskey, based upon costs (plus tax) of this magnitude.***

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* Pars. 46, 91.

** Complaint, pars. 47-51.

*** Complaint, par. 52.

Thus to pay the exaction at eight years in the hope of finding a later market would involve risks of loss far greater than even the total destruction of the spirits at eight years. To embark upon such a program would be courting economic suicide.*

In these circumstances the appellants and other members of the distilled spirits industry have no choice but to suffer immediate losses through

> (a) dumping the whiskey on the market under the threat of the force-out and for such prices as it will bring; or
>
> (b) the forced exportation of the whiskey at prices little better than the outright destruction; or
>
> (c) the forced destruction of the whiskey, either by redistilling the aged spirits and thus destroying substantially all of their value, or by simply pouring the whiskey down the sewer.**

Grave and irreparable damage had already been suffered by the appellants before the complaint in this case was filed a year ago. This had included the forced dumping of bottled whiskey at prices amounting to almost complete confiscation, a collapse in prices obtainable for their bulk whiskey to levels far below costs, a 65% loss in the market value of their whiskey inventories, and an almost 70% loss of profits. Similar damage had been suffered by other members of the distilled spirits industry.***

These drastic consequences of the force-out have been but the beginning. Far more drastic consequences are threatened for the immediately ensuing years.****

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* Complaint, par. 52.

** Complaint, pars. 54-75.

*** Complaint, pars. 55-62.

**** Complaint, pars. 63-75.

It is a virtual certainty that between now and 1959 the number of gallons of whiskey for which the industry will not have a market at any price, and which will therefore have to be destroyed, will be in excess of 50,000,000, and probably far in excess of that amount. The destruction of these more than 50,000,000 gallons of whiskey will entail a loss to the industry of the order of $100,000,000.* The appellants' share in these losses, as shown at page 9 above, will run into the millions of dollars.

The Bases for Appellants' Challenge of the Constitutionality of the Force-Out Provision.

The appellants contend that the force-out provision, as applied in the present circumstances, is an unconstitutional direct tax on property and a violation of due process of law. These contentions, outlined in the complaint,** were thoroughly briefed and argued before the District Court. The Court in its opinion expressed no view as to these issues. We set out below a brief statement of the appellants' position on these questions, before turning to the threshold issue upon which the District Court's decision turned: viz., the right to try these issues in a suit for injunction.

Unconstitutional property tax. Unlike the basic indirect consumption or marketing tax, the threatened levy of a direct tax at eight years depends solely upon the existence of the property on the tax payment date. Nothing that happened before, neither distillation nor warehousing nor aging, gave rise to any fixed or unavoidable obligation

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* Complaint, par. 65.

** Par. 15.

to pay any tax whatsoever. Nothing that may happen thereafter in any way diminishes the full impact of the tax upon the property and the ownership thereof. The eight-year exaction bears no relation to any action looking toward putting the spirits into the channel of trade. On the contrary, it in fact imposes a tax on property which never can or will be placed in the channels of trade, namely, the whiskey which would continue to evaporate after the tax payment date.*

The direct tax apportionment requirement set out in the Constitution (Article I, Section 2, clause 3 and Article II, Section 9, clause 4) constitutes and was intended to constitute a fundamental protection against oppressive taxation of property. We believe that the clear import of the long line of decisions by this Court bearing upon the point is that this protective apportionment requirement is fully applicable here, bearing particularly in mind that the oppression in this case extends even to forcing the outright destruction of the property.

Violation of due process of law. Turning now to the appellants' contention that the force-out provision as applied in the present circumstances is a violation of due process of law: The very essence of due process of law is that no man shall be deprived of his property unless there is a reasonable and proper public purpose to be served thereby. This fundamental guaranty is a limitation upon the federal taxing power as well as any other power. The test is the familiar one of balancing any public interest to be served against the resulting harm to the individual.

On the facts of this case, there can be no doubt that the force-out provision does grave damage to private interests. The drastic impact upon the appellants themselves

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* Complaint, pars. 33-34, 47.

is by no means an isolated instance. As the complaint clearly shows, the destructive impact of the provision is industry-wide.*

This destruction is wholly wanton. It is without justification from any revenue or other public standpoint. The government, far from gaining anything, actually loses hundreds of millions of dollars of revenue by reason of the continued threat of enforcement of the provision. Indeed, a limitation upon the bonding period has at no time even been considered by the Congress as creating any revenue. Originally enacted (as a one-year period) to serve a wholly different function which had become unnecessary even before the present eight-year period was adopted in 1894, the force-out provision from any revenue or other standpoint is an anachronism.**

Neither serving nor intended to serve any revenue or other public purpose in any way justifying the destruction wrought by it in the present circumstances, the force-out provision is a violation of due process of law under numerous decisions of this Court.

The complaint raises grave constitutional issues, and the District Court in no way suggested otherwise.

Turning now to the threshold issue before this Court on this appeal:

The Questions Are Substantial.

The District Court based its dismissal of the complaint solely upon the proposition that Section 7421 of the Internal Revenue Code of 1954 prohibits the maintenance of this action. The purpose of Section 7421, as this Court has held, is to protect against interference with the collection

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* Pars. 54-75.

** Complaint, pars. 79-92.

of revenue for the support of the government; the Section prohibits the maintenance of a suit for injunction only where there is a revenue consideration to justify such limitation upon the equity powers of the Courts. The decision below, however, is without justification from any revenue standpoint. The force-out provision does not produce revenue; it destroys it. The injunction sought would promote, not interfere with, the collection of revenue.*

The decision below is further without justification from any equity standpoint. Quite the contrary, the decision is a warrant for the destruction of appellants' property—millions of dollars worth of it. No matter how clearly unconstitutional the force-out provision may in fact be, the decision leaves the appellants with no choice but to continue to destroy their property under the threat of that provision, day after day and for the indefinite future.**

We think that the District Court, guided by the form and not the substance, has given to Section 7421 a meaning and application never intended by the Congress and never ascribed to it or any predecessor provision by this or any other Court. The grave issues raised on this appeal are obviously of the most pressing importance to the appellants. They are of equal importance to the entire United States distilling industry. They are the concern of every taxpayer in this country. The Treasury, far from gaining any revenue under the challenged force-out provision, is in fact losing hundreds of millions of dollars by reason of the continued threat of the exaction.***

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* Pages 11-12, 18 above.

** Pages 9, 14-16 above.

*** Page 18 above.

Section 7421 is Inapplicable Because the Injunction Sought Would Not Interfere With the Collection of Revenue.

The District Court, proceeding on the premise (Op. 3) that the injunction sought would "restrain the collection of a tax", directed practically all of its opinion to considering whether the appellants have shown "special and extraordinary circumstances" warranting an exception to Section 7421. The District Court concluded that such circumstances had not been shown. We think that conclusion demonstrably unsound, as shown at pages 24-32 below.

The issue at the outset, however, is the validity of the District Court's basic premise. The Court did not in any way suggest that, in fact, the injunction sought would interfere with the collection of revenue for the support of the government. Indeed, nowhere in the opinion is there even any reference to the specific facts, set forth in detail in the complaint, showing that the force-out provision has never been considered by the Congress as creating any revenue, and that at the present time the threat of exaction of tax at eight years actually reduces the revenue.*

It was never the intention of the Congress, in enacting Section 7421 of the Internal Revenue Code of 1954 and predecessor statutes, that the courts should be deprived of their usual equity jurisdiction simply on a showing that a measure is denominated a "tax". Nor has this Court ever so suggested at any time during the ninety-year history of these statutes. Quite the contrary, this Court has in each case looked beyond the labels and ascertained whether the injunction sought would in fact be inconsistent with the

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* Complaint, pars. 79-92.

Congressional objective of protecting against interference with the collection of revenue for the support of the government. In every case where it has appeared that no such revenue consideration was in fact involved, this Court has held the statutory prohibition inapplicable.

Miller v. *Standard Nut Margarine Co.*, 284 U. S. 498 (1932), is a leading example. There as in the present case the injunction sought was against the enforcement of a measure (oleomargarine tax) which was denominated a "tax". Unlike the Court below in this present case, however, this Court (pages 509-10) looked to the facts and considered them in the light of the Congressional purpose of protecting against interference with "the collection of revenues for the support of the government." The facts, this Court concluded, showed that a valid tax "could by no legal possibility have been assessed"; and it was accordingly held that the statutory provision was inapplicable because, on those facts, "the reasons underlying [the provision] apply, if at all, with little force."

In the present case it is even clearer than in the *Standard Nut Margarine* case that the reasons underlying the statute have no application. Here the challenged "tax" produces neither a valid nor an invalid increase in the revenues. Whether the force-out provision be in fact constitutional or unconstitutional, the continued threat of its enforcement is diminishing, not increasing the revenues.

Indeed, this Court has gone even further in manifesting its concern that the statutory prohibition shall be restricted to those instances where such limitation upon the equity powers of the courts is justified by a clear revenue consideration. In numerous cases where (unlike the present case) the injunction sought would actually deprive the Treasury of money, this Court has nevertheless held the statutory limitation inapplicable because the facts showed that the

Congress had imposed the exaction for purposes other than the ordinary tax purpose of providing revenue for the support of the government. *Hill* v. *Wallace*, 259 U. S. 44 (1922); *Mulford* v. *Smith*, 307 U. S. 38 (1939); *Lipke* v. *Lederer*, 259 U. S. 557 (1922); *Regal Drug Co.* v. *Wardell*, 260 U. S. 386 (1922); *R. C. Tway Coal Co.* v. *Glenn*, 298 U. S. 238 (1936). Among the numerous instances in which the lower courts have for a like reason held the statutory prohibition inapplicable, the following are examples: *Tovar* v. *Jarecki*, 173 F. 2d 449 (7th Cir. 1949); *Fontenot* v. *Accardo*, 278 Fed. 871 (5th Cir. 1922); *Liberis* v. *Nee*, 10 F. Supp. 336 (N. D. Fla. 1935).

We respectfully submit that the District Court failed to take proper cognizance of the crucial significance of the foregoing decisions of this Court and the lower courts. The District Court simply stated without discussion (Op. 6) that "the tax on distilled spirits" is not a penalty. It made no reference to the appellants' specific allegations showing that the force-out provision has never been considered by the Congress as either creating or protecting revenue, and that the provision has no purpose or effect other than to impose a confiscatory penalty on the continued ownership of distilled spirits beyond eight years.* It cited a single case, *United States* v. *Rizzo*, 297 U. S. 530, 533 (1936), which in no way involved the force-out provision and was directed to the general scheme of Internal Revenue taxation of distilled spirits. The appellants made it perfectly clear in their complaint that they are not challenging the "tax on distilled spirits". They are challenging only the anachronistic appendage known as the force-out provision which, unlike the taxing scheme in its basic and ordinary operation, has no revenue purpose or effect.**

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* Complaint, pars. 11, 79-92.

** Complaint, pars. 14-15.

The limited applicability of the statutory provision relating to injunctions is further shown by decisions in which this Court has held the provision inapplicable because the interference with the collection of revenues resulting from an injunction would be indirect and not direct. Thus in *Pollock* v. *Farmers' Loan & Trust Co.*, 157 U. S. 429 (1895), *rehearing*, 158 U. S. 601 (1895), where the injunction sought ran only against payment of the tax by the officers of the plaintiff stockholders' corporation and not directly against government officers, this Court permitted the litigation in an injunction suit of constitutional issues relating to the validity of an income tax statute. This result was reached despite the fact that the government appeared in the case and the decision on the merits (holding the tax measure invalid) was for all practical purposes binding on all.

To like effect, so far as the procedural aspects are concerned, is *Brushaber* v. *Union Pac. R. R.*, 240 U. S. 1 (1916).

In sum, this Court has never in any way suggested that Section 7421 or any predecessor provision is a blanket prohibition automatically foreclosing judicial scrutiny of the effects of every measure which a statute calls a "tax". This Court has in each case looked to the facts as to whether there was really any revenue consideration justifying such a limitation upon the equity powers of the judiciary. In every case where for any reason it has appeared that the injunction sought would not constitute a direct, immediate and clearly demonstrable interference with the collection of revenue exacted by the Congress for the usual tax purpose of supporting the government, this Court has held the statutory prohibition inapplicable. Conversely, in every case in which this Court or any lower court has held that Section 7421 or any predecessor provision was applicable so as to prohibit an injunction which would otherwise have

been granted, the facts clearly showed that the injunction sought would have constituted a direct interference with the flow into the Treasury of revenues exacted by Congress for the support of the government. Examples are *Graham* v. *du Pont*, 262 U. S. 234 (1923); *Dodge* v. *Osborn*, 240 U. S. 118 (1916); *Snyder* v. *Marks*, 109 U. S. 189 (1883); *Voss* v. *Hinds*, 208 F. 2d 912 (10th Cir. 1953); *Matcovich* v. *Nickell*, 134 F. 2d 837 (9th Cir. 1943); *McMullin* v. *Sheehan*, 95 F. 2d 129 (8th Cir. 1938).

In the present case the facts clearly show that there is no revenue consideration of any kind which would in any way justify any limitation upon the usual equity powers of the courts. Section 7421 is wholly inapplicable.

Even If, Contrary to the Fact, the Appellants Were Seeking to Enjoin the Collection of a Tax, Section 7421 Would Not be Applicable in the Special and Extraordinary Circumstances of This Case.

As shown above Section 7421 is inapplicable in this case for the reason at the outset that the appellants do not seek to interfere with the collection of revenue for the support of the Government.

But even if the force-out provision were in fact a "tax" within the meaning of Section 7421, that provision would not deprive the courts of equity jurisdiction in the special and extraordinary circumstances of this case.

Section 7421 and predecessor provisions are merely a codification of the usual rule that in order to invoke equity jurisdiction, there must be, in addition to a legal cause of action, special and extraordinary circumstances "sufficient to bring the case within some acknowledged head of equity jurisprudence." That was this Court's clear and definitive interpretation in the leading case of *Miller* v.

Standard Nut Margarine Co., 284 U. S. 498 (1932). Upholding the granting of injunctive relief against enforcement of a federal oleomargarine tax, this Court there held (page 509) that:

(a) the statutory provision is merely declaratory of the principle "that a suit will not lie to restrain the collection of a tax upon the sole ground of its illegality;" and

(b) the statutory provision does not abrogate the "salutary and well established rule" that "in cases where complainant shows that in addition to the illegality of an exaction in the guise of a tax there exist special and extraordinary circumstances sufficient to bring the case within some acknowledged head of equity jurisprudence, a suit may be maintained to enjoin the collector."

Those principles had been referred to by this Court in earlier cases. *Dodge* v. *Osborn*, 240 U. S. 118, 122 (1916); *Hill* v. *Wallace*, 259 U. S. 44, 62 (1922); *Bailey* v. *George*, 259 U. S. 16-20 (1922); *Graham* v. *du Pont*, 262 U. S. 234, 256, 257 (1923). They have been reiterated with approval by this Court, and applied by the lower courts, in numerous later cases. *Allen* v. *Regents*, 304 U. S. 439, 448-9 (1938); *Midwest Haulers* v. *Brady*, 128 F. 2d 496, 499 (6th Cir. 1942); *John M. Hirst & Co.* v. *Gentsch*, 133 F. 2d 247, 248 (6th Cir. 1943); *Mitsukiyo Yoshimura* v. *Alsup*, 167 F. 2d 104, 106 (9th Cir. 1948); *Sanders* v. *Andrews*, 121 F. Supp. 584, 593-95 (W. D. Okla. 1954), *rev'd* on other grounds, 225 F. 2d 629 (10th Cir. 1955); *Long* v. *Kelly*, 100 F. Supp. 235, 236 (M. D. Ala. 1951); *Driscoll* v. *Jones*, 19 F. Supp. 792, 794 (N. D. Okla. 1937). Within the past six months it has been held in another case that the very constitutional issues involved in this present case may properly be tried in an injunction suit; and the preliminary injunction

granted in that case was later dissolved only because of failure to post a required additional injunction bond. *Pabst* v. *Campbell, et al.*, Civil No. 1P56-C-226, S. D. Indiana, October 5, 1956.

The cases show that the special and extraordinary circumstances which may justify an exception to the statutory provision are by no means limited to any particular kind of situation; they are as broad and all-inclusive as equity jurisdiction itself.

In *Allen* v. *Regents*, 304 U. S. 439 (1938), a principal consideration was the fact that a test of the constitutional issues by any procedure other than an injunction suit could have been undertaken only at the risk of substantial penalties if those challenging the exaction should ultimately prove to be wrong on the merits.

In *Hill* v. *Wallace*, 259 U. S. 44 (1922), a principal consideration to which this Court pointed was that trial of the issues in an injunction suit would prevent a multiplicity of actions.

In numerous cases involving the validity of the processing taxes imposed under the Agricultural Adjustment Act of 1933 and amendments thereto, the courts entertained suits for injunction on the principal ground that under the applicable refund procedures there were burden of proof requirements which would pose practical difficulties in establishing a right to a refund. *A. P. W. Paper Co.* v. *Riley*, 12 F. Supp. 738 (N. D. N. Y. 1935); *Gold Medal Foods* v. *Landy*, 12 F. Supp. 406 (D. Minn. 1935); *Baltic Mills Co.* v. *Bitgood*, 12 F. Supp. 132 (D. Conn. 1935); *G. B. R. Smith Milling Co.* v. *Thomas*, 11 F. Supp. 833 (N. D. Tex. 1935); *Inland Milling Co.* v. *Huston*, 12 F. Supp. 554 (S. D. Iowa 1935).

In *Pocahontas Fuel Co.* v. *Early*, 13 F. Supp. 605 (W. D. Va. 1935), involving a challenge of the constitutionality

of the Bituminous Coal Conservation Act, a principal consideration was the fact that the suit for injunction afforded a speedier remedy. The court pointed out that the amount of the taxes which the plaintiff in that case would have had to pay during the time that it would have taken to get a decision in a refund suit would be so great as in and of themselves to jeopardize the plaintiff's business, regardless of what the ultimate decision on the merits might be.

In still other cases, the special and extraordinary circumstances held to justify an exception to the statutory provision consisted primarily in an inability to pay the tax and a resulting threatened destruction of property. *Miller* v. *Standard Nut Margarine Co.*, 284 U. S. 498 (1932); *Midwest Haulers* v. *Brady*, 128 F. 2d 496 (6th Cir. 1942); *John M. Hirst & Co.* v. *Gentsch*, 133 F. 2d 247 (6th Cir. 1943); *Mitsukiyo Yoshimura* v. *Alsup*, 167 F. 2d 104 (9th Cir. 1948); *Leonardi* v. *Goldberg*, 76 F. Supp. 747 (D. N. J. 1941); *John A. Gebelein, Inc.* v. *Milbourne*, 12 F. Supp. 105 (D. Md. 1935); *Long* v. *Kelly*, 100 F. Supp. 235 (M. D. Ala. 1951); and *Driscoll* v. *Jones*, 19 F. Supp. 792 (N. D. Okla. 1937). On the other hand, inability to pay was not alleged and thus played no part in numerous other cases where the right to maintain a suit for injunction was upheld. In many of these cases, indeed, it affirmatively appeared that those seeking injunctive relief were unquestionably in a position to pay the exaction. *Allen* v. *Regents*, 304 U. S. 439 (1938); *Rickert Rice Mills, Inc.* v. *Fontenot*, 297 U. S. 110 (1936); *Hill* v. *Wallace*, 259 U. S. 44 (1922); *Lipke* v. *Lederer*, 259 U. S. 557 (1922); *Regal Drug Co.* v. *Wardell*, 260 U. S. 386 (1922); *A. P. W. Paper Co.* v. *Riley*, 12 F. Supp. 738 (N. D. N. Y. 1935); *Gold Medal Foods* v. *Landy*, 11 F. Supp. 65, 12 F. Supp. 406 (D. Minn. 1935); *Baltic Mills Co.* v. *Bitgood*, 12 F. Supp. 132 (D. Conn. 1935); *In re Processing Tax Case*, 13 F. Supp. 218 (W. D. Tex. 1935);

Neild Mfg. Corp. v. *Hassett*, 11 F. Supp. 642 (D. Mass. 1935); *Inland Milling Co.* v. *Huston*, 11 F. Supp. 813, 12 F. Supp. 554 (S. D. Iowa 1935); *Danahy Packing Co.* v. *McGowan*, 11 F. Supp. 920, 12 F. Supp. 457 (W. D. N. Y. 1935).

We do not contend that the special and extraordinary circumstances in the present case are necessarily analogous in all respects to those which have been held to justify an exception in any particular earlier case. We do say that the cases clearly show that this Court and the lower courts have consistently and often applied the principle clearly laid down by this Court in the *Standard Nut Margarine* case (pages 24-25 above), viz.: that where special and extraordinary circumstances are shown, sufficient to bring a case within "some acknowledged head of equity jurisprudence", a suit for injunction may be maintained. And we do say that on the facts of this case there can be no question that that standard is met here.

As shown at pages 14-15 above, the plain fact is that the appellants cannot pay this exaction. Payment is economically out of the question. So long as the defendant is in a position to continue to threaten enforcement of the exaction, the appellants will have no choice but to continue to suffer the irreparable damage and destruction, in ever-increasing amounts.

From the standpoint of protection against the harm which the appellants now seek to enjoin, pursuit of refund claims previously filed, as suggested by the District Court (Op. 10), would be futile. Pursuit of such claims, relating to whiskey which reached the force-out date in the past, would in no way stop or even mitigate the irreparable damage and destruction with which the appellants are now faced in respect of whiskey which will reach the force-out date in the future. It is that damage and destruction,

threatened for the future, against which the appellants now seek the protection of the Courts. That damage and destruction would go on, unabated, throughout the long period of time that it would take to get an ultimate determination of the constitutional issues through any refund route.

Only through the speedy injunctive remedy afforded by 28 U. S. C. §§2284 and 1253 (1952), providing respectively for hearing at the earliest practicable date and for direct appeal to this Court from either the granting or denial of relief, can the appellants be protected in respect of any portion of the harsh consequences of the force-out provision. So urgent is the need for a speedy ultimate determination of the constitutional issues that the appellants have not even sought a temporary injunction, with its attendant procedural delays.

Recognition that Section 7421 is inapplicable in these circumstances will in no way affect the full applicability of that provision in the usual tax case, where such accumulating irreparable harm is not present. The present case is unique in that regard. The District Court's expressed fear (Op. 10) that trial of the issues in this case in an injunction proceeding would set a precedent rendering Section 7421 "meaningless" is without foundation.

Indeed, the circumstances in this case are so special and extraordinary that the application of Section 7421 so as to deny to the appellants the hearing which they seek is in and of itself a violation of due process of law. The District Court's decision is nothing less than a warrant for the destruction of millions of dollars worth of the appellants' property, without any opportunity for them to be heard as to the constitutionality of the purported tax provision which wreaks that destruction upon them.

The theoretically available remedy of paying the exaction and suing for refund is in fact no remedy at all. It could be pursued only at the risk of still further damage so oppressive as necessarily to intimidate the appellants from asserting their constitutional rights at all. Being thus intimidated from challenging the constitutionality of the force-out provision by that refund route, the appellants (under the District Court's decision) have no choice but to go on destroying their property under the threat of the force-out provision, to all practical intents and purposes as if the provision were constitutional.

The decisions of this Court clearly show that the Constitution forbids any statutory scheme whereby, as in the present posture of this case, a person gravely harmed by a statutory provision can challenge the constitutionality of that provision only at the peril of still greater harm if he proves to be wrong on the merits. *Cotting* v. *Kansas City Stock Yards Co.*, 183 U. S. 79 (1901); *Ex parte Young*, 209 U. S. 123 (1908); *Oklahoma Operating Co.* v. *Love*, 252 U. S. 331 (1920); *Terrace* v. *Thompson*, 263 U. S. 197 (1923).

The *Cotting* case involved a statute for the regulation of public stockyards; the *Young* case a railroad rate act; the *Love* case a regulatory scheme relating to laundry establishments; and the *Terrace* case a statute prohibiting the conveyance of land to aliens. In each case those adversely affected by the statute could of course have simply accepted its consequences without any test of its validity, just as the appellants in the present case can go on destroying their property under the threat of the force-out provision. In each of the foregoing cases, those adversely affected by the statute had the theoretical alternative of forcing an adjudication of their rights, but at the risk of large penalties if they proved to be wrong on the merits—just as in the present case it would be theoretically open to the applicants to pay the exactions and sue for a refund, under penalty of huge

additional losses if they should prove to be wrong on the merits.

While the precise nature of the penalties differed from case to case, the test applied by this Court was in each case the practical one: Are the risks attendant upon an unsuccessful pursuit of the theoretically available remedy so great "as might well deter even the boldest and most confident"? *Oklahoma Operating Co.* v. *Love*, 252 U. S. 331, 336 (1920). We respectfully submit that there can be no doubt that that test is met in this case. By no stretch of the imagination could the Directors of Schenley Industries, Inc., a publicly owned corporation whose stock is listed on the New York Stock Exchange, undertake to pay, or cause its subsidiaries to pay, this huge exaction in respect of the millions of the gallons of whiskey for which there will be no market, knowing as they do that if the constitutional issues should ultimately be decided against them, the losses of stockholders' money would be millions of dollars greater than even the outright destruction of the property now.

The District Court's opinion reflects no consideration of these grave issues concerning the very constitutionality of holding Section 7421 applicable in this case. The huge additional losses which would be the penalty for an unsuccessful pursuit of the theoretically available refund remedy were dismissed by the District Court (Op. 10) as resulting from appellants' "own course of conduct" and not from any illegal or unconstitutional act of the defendant. We respectfully submit that this wholly misconceives the issue. The appellants do not seek an injunction against the harm which would result from an unsuccessful pursuit of the refund remedy. For the very reason that that harm, whatever its source direct or indirect, would in fact be so great that as a practical matter appellants cannot and are not going to follow that course, there is no issue as to whether that harm would or would not be attributable to

the defendant. What appellants seek is protection against the destruction of their property, which necessarily results from the threatened enforcement of the force-out provision. Nobody questions that that threat is the defendant's own act.*

Conclusion.

The questions presented by this appeal are substantial and of urgent importance to both private and public interests. It is respectfully submitted that probable jurisdiction should be noted.

Respectfully submitted,

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Dated: February 15, 1957

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* The two cases cited by the District Court (Op. 10) in this connection, *Parker* v. *Winnipiseogee Lake Cotton and Woollen Co.*, 67 U. S. 545, 551 (1862), and *Coty* v. *Prestonettes, Inc.*, 285 Fed. 501, 514 (2d Cir., 1922) were far afield on their facts and we have been unable to find in those opinions any statements which appear to have any relevance here.

APPENDIX A

UNITED STATES DISTRICT COURT

FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Civil Action

No. 14,314

SCHENLEY DISTILLERS, INC. and
JOSEPH S. FINCH AND COMPANY,
Plaintiffs,

v.

JOHN H. BINGLER, United States District Director
of Internal Revenue for the
Pittsburgh Internal Revenue District,
Defendant.

Before STALEY, Circuit Judge, and MILLER and McILVAINE, District Judges.

OPINION OF THE COURT.

(Filed October 18, 1956)

By STALEY, Circuit Judge.

This suit in equity was commenced by Schenley Distillers, Inc., a Delaware corporation, and Joseph S. Finch and Company, a Pennsylvania corporation, against John H. Bingler,[1] the United States District Director of Internal Revenue for the Pittsburgh Internal Revenue District. The plaintiffs, who are distillers, owners, or warehousemen

[1] Bingler was substituted for a former Director who was the original defendant.

of whiskey and other distilled spirits stored in bond in Internal Revenue Bonded Warehouses, and both wholly-owned subsidiaries of Schenley Industries, Inc., requested that the defendant be permanently enjoined from determining or collecting the federal tax on any distilled spirits presently or hereafter in bond, in which they have an interest, unless and until the said distilled spirits shall be voluntarily withdrawn from bond. Because the requested injunctive relief is grounded upon allegations that the threatened collection of federal taxes as provided by an Act of Congress would be repugnant to certain provisions of the Constitution of the United States, the application for relief has been considered, pursuant to statutory requirement, 28 U. S. C. §§2282, 2284 (1952) by a three-judge court.

We are presently concerned with the defendant's motion, upon which argument has been heard, that the complaint be dismissed for various reasons. These are that the tax laws attacked are constitutional; that the plaintiffs have an adequate remedy at law; that this court does not have jurisdiction to issue an injunction restraining the collection of the taxes; that the plaintiffs should not be heard to attack the conditions of a statute under which they have obtained and are enjoying privileges; and that the complaint fails to state sufficient facts upon which relief can be granted.

The laws[2] which govern the taxation of distilled spirits and which are relevant in this case provide that there is "imposed on all distilled spirits * * * produced * * * in * * * the United States an internal revenue tax at the rate of $10.50 on each proof gallon." "The tax shall attach to distilled spirits * * * as soon as this substance is in existence as such * * *." A distiller, however, is not required to pay the tax at the time of the production of distilled spirits. After distillation, the spirits are deposited in locked tanks known as receiving cisterns. Under certain circumstances,

[2] The pertinent sections of the Internal Revenue Code of 1954 are 5001, 5002, 5003, 5004, 5005, 5006, 5011, 5173, 5193, 5194, 5231, 5232, 5242, 5302. Similar provisions were in the Internal Revenue Code of 1939.

however, the spirits are deposited in bonded warehouses for aging and in such circumstances the tax must be paid before the spirits are withdrawn from the warehouses. *In any event, however, the tax must be paid within eight years from the date of the original entry into the warehouse.* The tax, when paid, is paid upon the actual number of gallons in existence, which amount is lower than the amount originally deposited in the warehouse. This is because losses during storage will occur from various causes, such as soakage, leakage, evaporation, casualty, or theft. Under certain specified circumstances, the tax on the spirits is never collectible: if the spirits are voluntarily destroyed, or redistilled, or withdrawn for export.

The plaintiffs, in asking that this court enjoin the collection of the tax on their distilled spirits unless and until they are voluntarily withdrawn from bond, have in effect requested that we enjoin the enforcement of that provision of the law which requires that, regardless of voluntary withdrawal from bond, the tax must be paid within eight years of the deposit in bond.

In considering such interference with the collection of taxes as provided by Congress, we are faced immediately with Section 7421 of the Internal Revenue Code of 1954. That section provides, with certain exceptions that do not concern us, that "* * * no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court." To grant plaintiffs' request would clearly restrain the collection of a tax, and thus, if Section 7421 is applicable to this case, we must deny the requested relief.

This provision, which has been in the law for over eighty-five years, reads as though an injunction restraining the collection of taxes is not permitted under any circumstances. There have been situations, however, in which the Supreme Court of the United States has held that provision was not applicable and an injunction was permissible. So far as we have been able to discover, with just one exception, those cases in which the injunctions restraining gov-

ernment officials have been permitted were all cases in which the Court held that the purported tax sought to be restrained was in reality not a tax but a penalty, and the Court said that the statutory prohibition did not apply to the collection of penalties. *Lipke* v. *Lederer*, 259 U. S. 557 (1922); *Hill* v. *Wallace*, 259 U. S. 44 (1922); *Regal Drug Corp.* v. *Wardell*, 260 U. S. 386 (1922); *Mulford* v. *Smith*, 307 U. S. 38 (1939); see also *Allen* v. *Regents of the University System of Georgia*, 304 U. S. 439 (1938).

In *Hill* v. *Wallace*, 259 U. S. 44 (1922), the Court granted an injunction against the collection of taxes and said that an injunction could be granted in a case apparently within the terms of the statutory prohibition if there were present "extraordinary and entirely exceptional circumstances." 259 U. S. at page 62. The Court, however, in a later case denying an injunction, in an opinion written by Chief Justice Taft who also wrote the *Hill* opinion, interpreted the *Hill* case as one which should in fact be classed as a case involving a penalty in the form of a tax. *Graham* v. *DuPont*, 262 U. S. 234, 257-258 (1923). Thus, up to the time of the *Graham* decision, the cases in which injunctions were permitted involved penalties rather than taxes, although the Supreme Court had said several times that even the collection of a tax could be enjoined under extraordinary and exceptional circumstances.

Eventually, in *Miller* v. *Standard Nut Margarine Co.*, 284 U. S. 498 (1932), a factual situation was presented which warranted an injunction against the collection of taxes even though the tax was not considered a penalty as in prior decisions. In that case, an injunction restraining the imposition and collection of oleomargarine taxes on a product known as "Southern Nut Product" was permitted. The Court stated, at page 509, "in cases where complainant shows that in addition to the illegality of an exaction in the guise of a tax there exist special and extraordinary circumstances sufficient to bring the case within some acknowledged head of equity jurisprudence, a suit may be maintained to enjoin the collector." The special and

extraordinary circumstances were discussed by the Court, which said:

> "• • • A valid oleomargarine tax could by no legal possibility have been assessed against [complainant], and therefore the reasons underlying §[7421] apply, if at all, with little force. LeRoy *v.* East Saginaw Ry. Co., 18 Mich. 233, 238-239. Kissinger *v.* Bean, Fed. Cas. 7853. [Complainant] commenced business after the product it proposed to make had repeatedly been determined by the Commissioner and adjudged in courts not to be oleomargarine or taxable under the Act, and upon the assurance from the Bureau that its product would not be taxed. For more than a year and a half [complainant] sold its product relying upon the aforesaid rulings that it was not subject to tax. If required to pay the tax its loss would be seven cents per pound. Before the Commissioner's latest ruling [complainant] had made and sold so much that the tax would have amounted to more than it could pay. [The Commissioner] acquiesced in the injunctions granted [in other cases] and did not assess any tax upon identical products contemporaneously being made by complainants in such suits, and directed enforcement against [this complainant's] entire product. Such discrimination conflicts with the principle underlying the constitutional provision directing that excises laid by Congress shall be uniform throughout the United States. It requires no elaboration of the facts found to show that the enforcement of the Act against [complainant] would be arbitrary and oppressive, would destroy its business, ruin it financially and inflict loss for which it would have no remedy at law. It is clear that, by reason of the special and extraordinary facts and circumstances, §[7421] does not apply. The lower courts rightly held [complainant] entitled to the injunction." 284 U. S. at pages 510-511.

To our knowledge, the *Standard Nut Margarine* case is the only case, and no other has been cited by counsel,[3] in which the Supreme Court clearly held that although no penalty was involved, the circumstances were so special and extraordinary as to render inapplicable the statute prohibiting the maintenance of a suit to restrain the collection of taxes.

In the light of the Supreme Court decisions, Section 7421 prohibits the issuance of an injunction in this case, unless either the tax sought to be enjoined is in reality a penalty or the necessary special and extraordinary circumstances are present. Certainly, the tax on distilled spirits is not a penalty. *United States* v. *Rizzo*, 297 U. S. 530, 533 (1936). Thus, this court has jurisdiction to issue the requested injunction only if the requisite special and extraordinary circumstances are presented, in addition, of course, to the illegality of the exaction, with which we need not now concern ourselves.

The complaint in this suit is very lengthy, covering thirty-nine printed pages, most of which are devoted to facts concerning the entire distilled-spirits industry and the internal revenue laws applicable to the industry presently and historically. The factual allegations which specifically concern the plaintiffs are not many. The facts which follow are taken from the complaint and the submitted affidavits.

Because of the necessity for aging, distilled spirits are not marketed at the time of distillation but in later years. The industry, therefore, must estimate its needs in relation to the expected demands in the future. The requirement of the law that the tax on distilled spirits be paid within a certain time after deposit in warehouses has been

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[3] Plaintiffs have said that the principles laid down in the *Standard Nut Margarine* case were applied in *Allen* v. *Regents*, 304 U. S. 439 (1938). In the *Regents* case, however, although the court mentioned "extraordinary circumstances," it specifically held that the assessment and collection sought to be restrained was "not of a tax payable by respondent but of a penalty for failure to collect it from another." 304 U. S. at page 449.

in effect for many years although the time limits on payment have varied. Except for recent years, this time limitation was not of significant practical concern to the industry because it was always able to market its aged spirits before the deadline for payment of the taxes arrived.

In recent years, however, the industry has not been able to market its aged spirits before the eight-year tax payment deadline. It has had on hand millions of gallons of spirits upon which the tax became due but for which there was no market. The result has been an economic squeeze, resulting in financial losses. In some cases where the tax was paid, the industry, because of acute financial reasons, had to dump the spirits on the market and attempt to recoup what it had paid the government, and in doing so it had to forego profits and even suffer losses on its investment in the spirits.

In other cases rather than pay the tax, the industry has chosen to destroy, redistill, or export the aged spirits. But whichever course of action was followed, losses were suffered.

This situation will continue in the future since the tax payment deadline will be reached in the next several years on more spirits than can be profitably marketed.

Generally, plaintiffs claim that, along with the other members of the distilled-spirits industry, they face the dim prospect of severe economic loss in the future because of the fact that taxes must be paid on eight-year-old spirits whether or not a market exists. The relevant specific facts as to these plaintiffs is, of course, our important concern since they and not the industry are parties to this suit, and it is as to them that "special and extraordinary circumstances" must be found to exist.

As to the Joseph S. Finch Company, we know that during the first six months of 1956, almost one-quarter of its inventory which reached the eight-year deadline during that period was redistilled to escape the tax. Because of this, the loss suffered on 300,000 gallons of whiskey was about $500,000. Finch currently owns the remainder, after storage losses, of more than 25,000,000 original proof gal-

lons of distilled spirits in the Pittsburgh Internal Revenue District. The number of remaining proof gallons owned by Finch which will reach the age of eight years in bond in the future and for which we have figures are as follows: In the last half of 1956—1,650,000 gallons; 1957—2,558,000 gallons; 1958—4,213,000 gallons; and 1959—1,657,000 gallons. Finch will not have a normal market for all of these spirits at the time the tax is due, and so will have to decide whether to pay the tax and hold the spirits for an uncertain market or avoid the tax by destruction, redistillation, or exportation of the spirits.

So far as Schenley Distillers, Inc., is concerned, about all we know is that it is liable on a surety bond valued at $200,000 given to the government to guarantee payment of the tax on any distilled spirits deposited in one of the warehouses in the Pittsburgh Internal Revenue District, of which Schenley is the proprietor.

In the light of the above facts, we must determine whether either Schenley or Finch has shown that "special and extraordinary circumstances" exist as to it, sufficient to permit the issuance of an injunction.

As we have said above, Schenley's only interest and concern is that it might become liable on its surety bond of $200,000 if the tax on any distilled spirits deposited in the warehouse of which it is the proprietor is not paid as the law provides. There is no allegation that Schenley itself owns any distilled spirts. If the defendant is not enjoined from collecting taxes at the end of the eight-year period, Schenley might, in the future, have to make good if some owner of distilled spirits in Schenley's warehouse does not pay the tax due or take the permissible steps to avoid it. There is no allegation that there is any immediate threat that this will happen. We can speculate that it might, but that is hardly enough to warrant equitable interference in the collection of taxes.

Finch has argued that there do exist special and extraordinary circumstances which entitle it to equitable relief.

The basis for this contention is that an injunction is the only remedy which will protect it from irreparable harm.

We think, however, that the facts which have been presented to us are insufficient to warrant that conclusion. First of all, Finch has a remedy at law to test the constitutionality of the provision requiring payment of the tax within eight years. It can pay the tax at the end of eight years and sue for a refund.

Although we are told the number of gallons Finch owns which will reach the eight-year date in the next several years, we do not know what percentage of those amounts will be marketable and what percentage will not. We do know that in the first six months of 1956, one-quarter of Finch's eight-year-old spirits was redistilled. That percentage may or may not represent the total unmarketable eight-year spirits in that period. That percentage may or may not be indicative of how much of Finch's future eight-year inventory will be unmarketable. But, whatever the percentage of total inventory that will be unmarketable in the next several years, there are no facts alleged to support a conclusion that Finch will be financially unable to pay all the taxes as they become due, whether or not the spirits are marketable. Whatever financial statistics we have been given as to the total industry do not, of course, concern Finch. It simply cannot be said as to Finch on the facts before us that it could not afford to pay its taxes when due and sue for a refund even though there was no market for some of its spirits, for we know nothing of its anticipated sales in relation to its inventories, nor of its financial resources. There are no facts alleged to indicate that Finch could not afford to pay taxes and hold the spirits until the determination of its action at law.

If the collection of the tax at the eight-year period is held to be unconstitutional, Finch would recover its taxes paid and still have its spirits. The tax would then again be paid only when the spirits would be voluntarily withdrawn from bond and only upon the spirits remaining. We see no substantial difference between the situation thus described and the situation which would obtain if equity were to intervene and grant the relief sought by issuing a permanent injunction.

Finch claims, however, that it also runs the risk that if the tax be held constitutional in a suit for refund and Finch then has on hand unmarketable spirits upon which it has paid taxes, it would suffer greater loss than if it had chosen to destroy, redistill, or export the spirits rather than pay taxes. Such losses, it says, would be irreparable. This may be so, but the losses would result from Finch's own choice of a course of action permitted to it under the law. In effect, we are asked to extend equitable relief to enable Finch to avoid harm which would be caused not by any illegal or unconstitutional act of the defendant, but caused by plaintiff's own course of conduct. In such circumstances, equity will not act, as before harm to the defendant can be considered in determining the adequacy or inadequacy of a legal remedy, it must clearly appear that the source of the harm is the wrongful act of the defendant. See *Parker* v. *Winnipiseogee Lake Cotton & Woollen Co.*, 67 U. S. 545, 551 (1862); *Coty* v. *Prestonettes, Inc.*, 285 Fed. 501, 514 (C. A. 2, 1922); 43 C. J. S., injunctions, §19(a).

Plaintiffs have already instituted suits for refunds of taxes exacted under the eight-year provision of the law, in which suits, among other questions, they have raised the constitutionality of the eight-year provision. They allege, however, that the suits will not permit a determination of the constitutionality of the law as speedily as this proceeding. But if this were reason for considering the remedy at law inadequate, Section 7421 of the Internal Revenue Code of 1954 would become meaningless. And in this case especially, we should not consider the relative speed of the two proceedings because plaintiffs knew as early as 1952 of the imminency of the problem of excess supply over demand of eight-year-old spirits and could have filed refund claims at that time, yet they waited until the latter part of 1955 to file their first claim for refund. No reason for plaintiffs' inaction has been advanced. We are told merely that the delay was due to hope for Congressional relief.

This court is of the opinion that the facts of this case are not of such "special and extraordinary circumstances" as moved the Supreme Court to grant the injunction in the *Standard Nut Margarine* case. The facts are not such as to bring the plaintiffs under any acknowledged head of equity jurisprudence, as required in that case. For this reason, because of Section 7421, we cannot maintain this suit to restrain the collection of the federal taxes

The complaint will be dismissed.

Order.

And now, this 18th day of October, 1956, defendant's motion to dismiss the complaint will be and it hereby is granted. The complaint of plaintiffs, Schenley Distillers, Inc., and Joseph S. Finch and Company, which seeks to enjoin the defendant from determining and collecting federal taxes on distilled spirits unless and until they are voluntarily withdrawn from bond will be and it hereby is dismissed.

/Sgd/ Austin L. Staley,
Circuit Judge,

/Sgd/ John L. Miller,
District Judge,

/Sgd/ John W. McIlvaine,
District Judge,